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IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

No. 875

LYNDON A. DURANT, *Petitioner*,

v.

UNITED STATES OF AMERICA, *Respondent*.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

EUGENE GRESSMAN
1730 K Street, N. W.
Washington 6, D. C.

GEORGE D. CROWLEY
GERALD C. RISNER
135 South LaSalle Street
Chicago 3, Illinois

Counsel for Petitioner

February 28, 1964.

PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

INDEX

	Page
Citation to opinions below	1
Jurisdiction	2
Question presented	2
Statute involved	2
Statement of the case	3
Reasons for granting the writ	10
1. The decision below raises an important question in the criminal administration of the revenue laws as applied to normal modes of operation in the business world	10
2. The decision below conflicts with the relevant decisions of this Court and of other Courts of Appeals as to the standard to be applied in determining whether and to what extent negligence can be equated with willfulness under § 7201	13
Conclusion	19
Appendix A (Opinion and judgment of Court of Appeals)	1a
Appendix B (Special Findings and Opinion of District Court)	13a

CITATIONS

CASES:

Gaunt v. United States, 184 F. 2d 284 (C.A. 1) 17
Holland v. United States, 348 U.S. 121 16
Pappas v. United States, 216 F. 2d 515 (C.A. 10) 17
Spies v. United States, 317 U.S. 492 ..... 13, 16, 18
United States v. Allen, 44 Amer. Fed. Tax Rep. 894 (S.D. Cal., Nos. 20984-20984-4, 1950) 11, 12
United States v. Martell, 199 F. 2d 670 (C.A. 3) 17
United States v. Mollet, 290 F. 2d 273 (C.A. 2) 17
United States v. Murdock, 290 U.S. 389 ..... 16, 18
United States v. Pechenik, 236 F. 2d 844 (C.A. 3) 17, 18
United States v. Ragen, 314 U.S. 513 ..... 16, 18

STATUTES: Page

26 U.S.C. § 7201 ..... 2, 12, 13, 14
26 U.S.C. § 7203 14

MISCELLANEOUS:

Balter, The Line Between Negligence and Fraud, New York Univ. Twelfth Annual Institute on Federal Taxation (1954) 12
10 Mertens, Law of Federal Income Taxation (Zimet revision, 1958) 18

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

The petitioner respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit entered in the above-entitled case on November 6, 1963.

CITATION TO OPINIONS BELOW

The opinion of the Court of Appeals, affirming the conviction of petitioner, was rendered on November 6, 1963, and is reported at 324 F. 2d 859. It is reprinted in Appendix A hereto, p. 1a, *infra*. The findings of

fact and opinion of the District Court for the Northern District of Illinois, Eastern Division, dated October 1, 1962, are reported at 208 F. Supp. 890 and are reprinted in Appendix B hereto, p. 13a, *infra*.

JURISDICTION

The judgment of the Court of Appeals was entered on November 6, 1963. A timely petition for rehearing was denied on December 30, 1963. On January 20, 1964, Mr. Justice Clark signed an order extending the time for filing this petition to and including February 28, 1964. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

QUESTION PRESENTED

Whether, in a prosecution of an individual corporate executive for willful attempt to evade or defeat a personal income tax in violation of 26 U.S.C. § 7201, the requirement of willfulness can be proved merely by a series of negligent omissions to cure defective corporate accounting procedures where there is a complete absence of proof of any affirmative act of fraud, concealment or other bad faith or evil intent by the defendant.

STATUTE INVOLVED

This case involves Section 7201 of the Internal Revenue Code of 1954, 26 U.S.C. § 7201:

> Any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof shall, in addition, to other penalties provided by law, be guilty of a felony and, upon conviction thereof, shall be fined not more than $10,000, or imprisoned not more than 5 years, or both, together with the costs of prosecution.

STATEMENT OF THE CASE

A three-count indictment charged that petitioner did willfully attempt to defeat and evade a large part of the income tax due and owing by him and his wife to the United States for the calendar years 1954, 1955 and 1956. The alleged tax deficiencies for these three years totalled $142,714.00. The taxes actually paid aggregated $193,949.50.

Petitioner pleaded not guilty. He was tried, without a jury, by Judge Hubert L. Will of the District Court for the Northern District of Illinois, Eastern Division. Motions for judgment of acquittal were denied at the close of the Government's case and at the close of all the evidence. Petitioner was found guilty as charged. He was then sentenced to imprisonment for a period of 60 days on each count, the sentences to run concurrently, and fined $15,000 and costs. The judgment of conviction was affirmed on appeal by the Court of Appeals for the Seventh Circuit.

The District Court, pursuant to Rule 23(c) of the Federal Rules of Criminal Procedure, entered Special Findings of Fact (Appendix B hereto, pp. 13a-18a, *infra*) and an Opinion (Appendix B hereto, pp. 18a-23a, *infra*). Those Special Findings may be summarized as follows:

(1) Petitioner at all times was the president, chief executive officer and sole stockholder of United Manufacturing Company (hereinafter called "United"). Additionally, he was United's chief engineer, designer and electronic specialist.

(2) The tax returns for two of the three years in question were prepared by one Oettinger, vice president of United, the third return being prepared by an independent certified public accountant. Petitioner had delegated to Oettinger supervision of the cor-

poration's administrative affairs; and Oettinger was responsible for the keeping of all corporate books of account during the tax years.[1] One Taibleson, a certified public accountant, was United's controller during these years and, as such, was subordinate to Oettinger.[2] A Miss Croson, who also was subordinate to Oettinger, was in charge of accounts payable.[3]

(3) During the three years in question—1954, 1955 and 1956—United made expenditures for or on behalf of petitioner and for his personal economic benefit aggregating $815,021.08, of which $602,692.11 was charged to a personal account on the corporation's books entitled "L. A. Durant."[4] The remainder, total-

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[1] Oettinger testified that petitioner had never given him instructions as to how to charge any particular item on United's books. App. 338. Nor did Oettinger ever discuss his preparation of petitioner's tax returns with petitioner, save for one matter not here relevant. App. 340-342. As to the "L.A. Durant" account, Oettinger never reviewed the account in detail with petitioner. App. 338. He stated that "at various times Mr. Durant would ask me what the balance of the account was, and I would either go look or ask somebody to get the balance and gave it to him." App. 138.

[2] Taibleson also testified that petitioner had never advised or instructed him or any one else how bills should be charged on the company books. App. 59, 75. And he never reviewed the corporation's income tax returns with petitioner. App. 82.

[3] Both Miss Croson and Miss Warden, who handled the accounts payable and distributed the bills to the accounts to be charged, indicated in their stipulated testimony that they never asked petitioner and he never told them how to charge or how to handle any items to the accounts payable and the daily pay-outs. Whenever they had any questions they would ask Oettinger. App. 46-52.

[4] The stipulated facts showed that from its inception in 1946 through 1956, the "L.A. Durant" account had charges of $1,556,296.44 and credits of $1,488,480.92. App. 19. During the years 1954, 1955 and 1956, charges were made to this account totalling $602,692.11 and petitioner made repayments to the account totalling $612,510.20. App. 18-19; Def. Ex. 1.

ling $212,328.97, was charged to various corporate accounts and was not reported as income by the petitioner and his wife in their joint returns for the years in question. This $212,328.97 was distributable among the three years as follows:

1954	$ 51,716.17
1955	66,877.19
1956	93,735.61
Total	$212,328.97.

(4) Each of the expenditures by United reflected by the $212,328.97 figure had been recorded in the records of United either as expenses of the corporation and deducted by it as business expenses in its corporate tax returns or as an acquisition of an asset by United and thereafter depreciated, the depreciation being then deducted on the corporate tax returns. None of these expenditures, however, constituted a corporate expense or an acquisition of assets, all of them being for the personal economic benefit of petitioner.

(5) In December 1951 the corporate tax returns of United for the years 1949 and 1950 were examined by a revenue agent, Zivin. He questioned several categories of items in the corporation's books and records of account, one of which was the use of corporate funds for personal expenses. In the course of auditing the returns, Zivin "had several conferences at which both the defendant [petitioner] and Oettinger were present and in which the question of charging personal expenses to the corporation was discussed." Finding No. 10, p. 16a, *infra*. At the final conference on December 23, 1951, Zivin discussed all the questioned categories with petitioner and Oettinger and advised them that the practice of charging personal expenses to the corpo-

ration should be stopped. The petitioner "*replied that if there were personal expenses charged to the corporation, they should be charged to his personal account.*" Finding No. 10, p. 16a, *infra*.

(6) In February 1954 a second revenue agent, Wagar, examined United's returns for the years 1949 through 1953. He questioned the same categories questioned earlier by Zivin and disallowed substantial personal expenses of petitioner which had been charged to the corporation during these years. Wagar also had conferences with petitioner and Oettinger, informing petitioner that it was improper to charge personal expenses to the corporation "*although Agent Wagar did not discuss the specific items with the defendant [petitioner] but discussed them with Oettinger.*" Finding No. 11, pp. 16a-17a, *infra*.

(7) Neither petitioner nor anyone else instructed the controller Taibleson to make any changes in the bookkeeping or accounting practices of United after either agent's examination. On occasion, petitioner brought invoices or bills to Taibleson and directed him to pay them without designating any account to which they were to be charged. Without some specific direction to charge an item to petitioner's personal account, the District Court found, "it was the established practice of the corporation to charge such items to various corporate accounts." Finding No. 12, p. 17a, *infra*.

(8) On a number of occasions during the years 1954 through 1956 the petitioner instructed United's purchasing agent, Olson, to purchase merchandise for him. The District Court found that on no occasion did petitioner "instruct Olson to charge the purchases to his personal account and, pursuant to the established prac-

tice of the corporation, Olson charged such purchases to various corporate accounts." Finding No. 13, p. 17a, *infra*.[5]

As a result of the foregoing Special Findings, the District Court concluded that (a) petitioner knew at the time he filed his 1954, 1955 and 1956 income tax returns that he had taxably income as a result of these various payments by United for his personal economic benefit; (b) each of the tax returns for the three years was false when filed and petitioner knew them to be false; and (c) petitioner willfully and knowingly attempted to evade and defeat part of the income tax due and owing by him and his wife for each of the three years by knowingly and intentionally filing false returns in which he intentionally and falsely stated their joint taxable income and the income tax due thereon. Findings No. 14, 15, 16, pp. 17a-18a, *infra*.

In its Opinion, the District Court disposed of the contention that the corporate payments on petitioner's behalf could be considered as loans by ruling that the evidence indicated no intent or action which would support such a contention. See pp. 19a-20a, *infra*. The second contention, that petitioner did not have the requisite criminal intent, was rejected on two grounds:

First, as to claim that petitioner did not know that United was paying his personal expenses since he had delegated responsibility for maintenance of the books to subordinates, the court said that there was no evi-

[5] The court further found that on some occasions petitioner would instruct Olson to make purchases for a separate corporate project known as "Caravan" and would indicate that such purchases were to be charged to the Caravan account. See p. 17a, *infra*.

dence that petitioner, after the visits and advice of the two revenue agents, ever instructed his subordinates to change the practice of charging any bill or invoice submitted by him to a corporate account unless he specifically designated otherwise. But the District Court conceded that there was "no evidence that the defendant at any time instructed his subordinates to adopt this practice and to charge his personal expenses to corporate accounts." See p. 21a, *infra*.

The District Court found it difficult to believe, in light of the 2,572 personal items charged to corporate accounts over the three years, that petitioner was unaware of the manner in which they were being handled on the corporation's books. The court added that the fact that petitioner on occasion had personally issued corporate checks for personal expenses, without indicating to or advising his subordinates that the checks were in fact for personal expenses, added to the court's disbelief of petitioner's claimed ignorance. See p. 21a, *infra*.

Secondly, as to claim that if petitioner knew of the corporation's practices in this respect he did not know that the items were income to him that should be reported, the court concluded that since such items were similar in nature to the more than $105,000 of disallowed corporate expenses previously charged to him as income by the revenue agents in the prior audits he must have known the items here involved were also income to him. See pp. 21a-22a, *infra*.

The District Court then enunciated the test of willfulness by which it judged this case and by which it concluded that petitioner had willfully attempted to

evade a part of his income tax obligations for the years 1954-1956 (See p. 22a, *infra*):

> "Defendant here, however, after being warned by two revenue agents that the charging of personal expenses to corporate accounts and the failure to report such items as income in his joint returns was improper, made no change whatsoever in the challenged practices. What may have been negligence or mere understatement of income in the earlier years can hardly be so considered in later years after the agents' warnings. The only reasonable inference from defendant's conduct is that he deliberately and wilfully continued practices which he had been advised were improper and the effect of which was substantially to understate his taxable personal income.
>
> "There is a point of repetition at which action originally careless or negligent becomes deliberate and wilful. The defendant passed that point when, after warnings by two revenue agents, he did nothing but continue the improper and challenged practices."

In affirming the District Court's judgment, the Court of Appeals approved that court's determination as to petitioner's willfulness in the following language (pp. 9a-10a, *infra*):

> "Defendant submits that the most that can be inferred from the evidence in this case is a certain amount of laxity, but his counsel urges that any amount of laxity does not constitute the requisite willfulness.
>
> "As an abstract proposition, we would agree that no amount of laxity in and of itself constitutes willfulness. However, in the case at bar, we believe that the district court properly recognized the additional factors revealed by the records, tending to prove a willful intent: (a) defendant

knew the corporation was paying his expenses, (b) the payments were not considered loans by the parties, (c) defendant knew the corporate payments were income to him; and therefore properly found that defendant willfully failed to include them in his returns.

"As we have indicated, the events following the prior audits for 1949-1953 served to clearly warn defendant of his duty to report as his personal income the charges of indebtedness incurred by him and paid by the corporation. Moreover, his failure to indicate on many of the expenditure vouchers any notation indicating appropriate classifications leading to a proper charge to him personally, also tends to support the finding of willfulness.

"His continuous failure to see that the warnings of Zivin and Wagar were heeded might reasonably be expected to result in a continuation of the practice of charging his personal obligations to the corporation."

REASONS FOR GRANTING THE WRIT

1. The decision below raises an important question in the criminal administration of the revenue laws as applied to normal modes of operation in the business world.

In this modern day when busy corporate executives frequently charge personal expenses in the first instance to their corporations, leaving to their administrative subordinates the task of properly allocating those expenses to their personal accounts on the corporate books, it becomes important to resolve the recurring question of their criminal responsibility for improper and negligent bookkeeping practices.

Is such a corporate executive to be held guilty of willfully attempting to evade his own income tax obligations because of the derelictions of those to whom he delegated the functions of keeping the corporate

records in proper order? Must he, despite any lack of accounting or bookkeeping expertise, affirmatively enter into the day-to-day ministerial function of seeing to it that a particular personal expense is charged to his personal rather than a corporate account on the ledger book? Does he subject himself to criminal sanctions by doing no more than repaying from time to time the amounts which his subordinates tell him he owes on his personal account, amounts later found to be incomplete or imperfect?

These questions arise in the context of a case where there is a total absence of any finding of willfulness or criminal intent other than what has been deduced from a feeling that petitioner was negligent over a period of time. Willfulness has been found not from what petitioner actually did but from what he should have done. What he actually did was no more than what most executives do—charge personal expenses to the corporate treasury and trust that his subordinates will make the proper bookkeeping allocations and charge him with the proper personal expenses.

This case finds an almost exact parallel in *United States* v. *Allen*, 44 Amer. Fed. Tax Rep. 894 (S.D. Cal., Nos. 20984-20984-4, 1950), where Judge Yankwich set aside a jury verdict of guilty as to corporate executive who, "busy with other affairs, trusted to the bookkeeping of those he employed for the purpose of making a full and accurate account of the moneys". There, as here, the subordinates were unanimous in their testimony that the executive never told them "to falsify any record or to make any entry which did not conform to reality." There, as here, the facts as to the allocations actually made on the books were never called to the attention of the executive. And there,

as here, there was a complete absence of the factors usually found in cases of true willful criminal intent—"failure to keep books, destruction of records, deliberate instructions to persons keeping records not to make full disclosures and the like."

What Judge Yankwich concluded illustrates both the importance and the impropriety of inflicting criminal liability on a busy executive in such a situation (*Id.*, p. 896):

> "... in view of the large scope of his operations and the hundreds of thousands of dollars that went in and out of this one account in which was placed all the moneys coming to him whether derived from income as reimbursement, as money advanced from loans and other, knowledge cannot be imputed to him to the extent of making him criminally liable. Grant that this amounts to carelessness of the most gross kind. It is not sufficient to supply the criminal design which is the essence of this offense."

Moreover, the problem of the extent to which general corporate negligence can be translated into the specific willful intent necessary to convict the top executive of a violation of 26 U.S.C. § 7201 is important not only to the business community but to the proper administration of the revenue laws. As one commentator has said with respect to the administration of the civil penalties of the Revenue Code,[6]

> "Where the record discloses *gross negligence* or *reckless disregard* of the taxpayer's responsibility to file or to have someone else prepare and file a true tax return, the temptation to infer

[6] Balter, *The Line Between Negligence and Fraud*, New York Univ. Twelfth Annual Institute on Federal Taxation, p. 25 (1954).

> fraudulent intent from these facts is, of course, very understandable. It is in this area that we find the most acute disagreements between the Commissioner, the Tax Court and the various Courts of Appeals."

The same type of disagreement is even more acute and significant with respect to the criminal sanctions of the Code.

If the decision below stands without some definitive clarification of the problem by this Court, general corporate laxness means criminal liability for the executive officer. Corporate executives must then act in dire peril in following what has become a normal and accepted mode of operation in the business world. The implications of such a result merit the full consideration and attention of this Court.

2. The decision below conflicts with the relevant decisions of this Court and of other Courts of Appeals as to the standard to be applied in determining whether and to what extent negligence can be equated with willfulness under § 7201.

The decision of the court below to the effect that willfulness for purposes of 26 U.S.C. § 7201 can arise from long continued negligent practices with respect to corporate records is at war with the concept of criminal willfulness as developed by this Court and other Courts of Appeals.

Indeed, the opinion below is irreconcilable with the principles established by this Court in *Spies v. United States*, 317 U.S. 492, 498-499. The Court there indicated that by enacting what is now § 7201—"the gravest of offenses against the revenues"—Congress intended that there be proof of "some willful commission in addition to the willful omissions" punishable as

misdemeanors under what is now § 7203. There must thus be proof of "a willful and positive" or "affirmative" attempt to evade taxes rather than just a "passive neglect." But the court below ignored these principles in ruling that the repetition of negligence or "passive neglect" can reach a point where it becomes proof of deliberateness or willfulness, without some "positive" or "affirmative" act intervening.

The court below agreed, as "an abstract proposition," that no amount of laxity in and of itself constitutes willfulness for purposes of § 7201. It then proceeded to hold that more than laxity was involved here since (a) petitioner knew the corporation was paying his expenses, (b) the payments were not considered loans, (c) petitioner knew the corporate payments were income to him, (d) petitioner failed to heed prior warnings from revenue agents, and (e) petitioner failed to indicate proper classifications on many of his expenditure vouchers.

Those five factors, however, are either irrelevant to the question at hand or constitute no more than an extension of the laxity or negligence which the court conceded was inadequate to constitute willfulness. Factors (a), (b) and (c) merely reflect a practice, not challenged by the law, of charging personal expenses in the first instance to the corporation; the problem then becomes one of allocating the personal expenses to the personal account in the corporate books. Factor (e) is clearly of the negligent variety, indicating that petitioner should have been more careful with respect to voucher identifications.

It is factor (d) which was critical to the District Court's finding of wilfulness—a finding that petitioner

did not heed the agents' warning that charging personal expenses to corporate accounts was improper and that such items should have been reported as personal income. But the District Court itself found that when the first agent gave this warning petitioner "replied that if there were personal expenses charged to the corporation, they should be charged to his personal account." Finding No. 10, p. 16a, *infra*. And as to the second agent's warning, the court found that the agent "did not discuss the specific items with the defendant but discussed them with Oettinger." Finding No. 11, p. 17a, *infra*. The Court further found "no evidence that the defendant at any time instructed his subordinates to. . . charge his personal expenses to corporate accounts." See p. 21a, *infra*.

The improper bookkeeping practices then continued —without a shred of evidence that petitioner knew, let alone directed, that the warnings went unheeded by those subordinates responsible for the corporate accounting. He assumed, perhaps negligently, that Oettinger (who was present when the agents gave their warnings) would see to it that all of these items would be charged to his personal account. That assumption was reasonable to the extent that $602,692.11 was properly charged to his personal account during the three years in question, and $1,556,296.44 so charged over a ten-year period. App. 18-19; Def. Ex. 1.

Yet the District Court found, and the Court of Appeals agreed, that there "is a point of repetition at which action originally careless or negligent becomes deliberate and wilful" and that what "may have been negligence or mere understatement of income in the earlier years can hardly be so considered in later years after the agents' warnings." See p. 22a, *infra*. In

other words, negligence plus more negligence becomes willfulness for purposes of § 7201. Such a conclusion is contradicted by both the intent of § 7201 and the relevant appellate court decisions as to the concept of willfulness.

This Court in *United States* v. *Ragen*, 314 U.S. 513, 515, held that in a prosecution for willful attempt to evade or defeat a tax it must be shown that the acts complained of "were willfully done in bad faith and with intent to defeat the tax." And in *Spies v. United States*, 317 U.S. 492, 499, the Court indicated in a general way various forms of deceitful practices that would permit an inference of such bad faith—"keeping a double set of books, making false entries on documents, destruction of books or records, concealment of assets or covering up sources of income, handling of one's affairs to avoid making the records usual in transactions of the kind, and any conduct, the likely effect of which would be to mislead or confuse."[7]

Thus the requisite evil intent must involve some conscious effort to conceal or falsify. There must be something more than negligence, carelessness, misunderstanding or unintentional understatement of income. As this Court said in *United States* v. *Murdock*, 290 U.S. 389, 396:

> "Congress did not intend that a person, by reason of a bona fide misunderstanding as to his liability for a tax . . . *or as to the adequacy of the rec-*

[7] See also *Holland* v. *United States*, 348 U.S. 121, 139, where an inference by the jury of willfulness was permissible where there was evidence of a failure on petitioners' part "to include all of their income in their books and records," as well as a consistent pattern of underreporting of large amounts of income. In the instant case, all the personal expenditures were fully identifiable from the corporate records and the District Court made no findings as to any concealment of the expenditures.

> *ords he maintained,* should become a criminal by his mere failure to measure up to the prescribed standard of conduct." [Emphasis supplied.]

Reliance on the basic principles thus enunciated by this Court has led a number of Courts of Appeals to rule that mere negligence—even gross and repeated negligence—is not enough to establish willfulness under § 7201. See *Pappas* v. *United States,* 216 F. 2d 515, 519 (C.A. 10); *Gaunt* v. *United States,* 184 F. 2d 284, 291, n. 4 (C.A. 1); *United States* v. *Pechenik,* 236 F. 2d 844, 846 (C.A. 3). In the words of the Third Circuit, *United States* v. *Martell,* 199 F. 2d 670, 672, a willful evasion of a tax "requires an intentional act or omission as compared to an accidental or inadvertent one. It also requires a specific wrongful intent to conceal an obligation known to exist, as compared to a genuine misunderstanding of what the law requires or a bona fide belief that certain receipts are not taxable." In short, the Government must show some "affirmative action." *United States* v. *Mollet,* 290 F. 2d 273, 274 (C.A. 2).

The failure to find such "affirmative action" in this case and the resulting conflict with the foregoing cases are highlighted by the Third Circuit's decision in *United States* v. *Pechenik,* 236 F. 2d 844, 846, which, on substantially similar facts, reached the opposite result from that rendered below. In *Pechenik,* a corporate executive's conviction for having willfully understated the income and tax obligations of the corporation was reversed. There, as in this case, the executive had turned over the books, bookkeeping and preparation of tax returns to the bookkeeper and accountant. There, as here, there was no evidence that the executive ever interfered with the books or that he was in any way linked with the erroneous bookkeeping. All that

was left, as here, was the suggestion that the executive had been negligent, plus the expressed disbelief that the executive did not really know what had transpired on the corporate books. Negligence and incredulity, however, were ruled inadequate as "probative evidence linking the defendant with the erroneous books and tax returns in any manner which should result in his conviction of the offense charged." 236 F. 2d at 846. That conclusion in *Pechenik* cannot be squared with the one reached below.[8]

While the standard of willfulness admits of no inclusive or comprehensive definition, applicable to all cases, it does lend itself to a delineation which rejects negligent omissions to check on corporate bookkeeping operations. And to hold as the court did below, that a series of omissions, concededly negligent in nature at the start, can somehow reach the point where negligence ceases and willfulness begins—without any affirmative act of concealment, fraud or evil intent intervening—is to reach a result in conflict with the principles laid down by this Court in the *Ragen, Spies* and *Murdock* cases, as well as with the Third Circuit's ruling in *Pechenik*.

The importance of the question thus presented, combined with the clear conflicting decisions, justifies an invocation of this Court's review powers.

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[8] See 10 Mertens, Law of Federal Income Taxation (Zimet revision, 1958) § 55A.09: "A distinction must be drawn between carelessness of the 'most gross kind' and the 'criminal kind' which is the essence of the offense. . . . Before a conviction under the Code can be sustained the record must reveal probative evidence linking the defendant with the erroneous books and tax returns. Reliance upon the conduct of employees in good faith is not a punishable event. A mistake, standing alone, is not sufficient to sustain a conviction."

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari to review the judgment of the Court of Appeals for the Seventh Circuit should be granted.

Respectfully submitted,

EUGENE GRESSMAN
1730 K Street, N. W.
Washington 6, D. C.

GEORGE D. CROWLEY
GERALD C. RISNER
135 South LaSalle Street
Chicago 3, Illinois

Counsel for Petitioner

February 28, 1964.

APPENDIX A

IN THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 14005 SEPTEMBER TERM, 1963, SEPTEMBER SESSION, 1963

UNITED STATES OF AMERICA, *Plaintiff-Appellee,*

v.

LYNDON A. DURANT, *Defendant-Appellant.*

Appeal from the United States District Court
for the Northern District of Illinois, Eastern Division

November 6, 1963

Before HASTINGS, *Chief Judge*, and SCHNACKENBERG and CASTLE, *Circuit Judges.*

SCHNACKENBERG, *Circuit Judge.* Lyndon A. Durant, defendant, having been indicted under 26 U. S. C. A. § 7201 and charged in three counts with willfully attempting to defeat and evade a part of income tax due and owing by him and his wife to the United States of America, for the calendar years 1954, 1955, 1956, the deficiency totaling $142,714.40, pleaded not guilty and was tried by the court without a jury.

The court having denied defendant's motions for judgment of acquittal at the close of the government's case and at the close of all the evidence, defendant was found guilty on each count and judgment was entered accordingly. Defendant was sentenced to the custody of the attorney general for a period of 60 days on each count, the sentences to run concurrently, and fined $15,000 and costs. From said judgment defendant appealed to this court.

According to the stipulated proof, unreported income totaling $212,328.97 upon which the tax deficiency for the three years is computed, was derived from corporate expenditures of United Manufacturing Company, an Illinios

corporation, Chicago, Illinois, made for the personal benefit of taxpayer. The immediate beneficiaries of these expenditures, other than defendant personally, are identified in the stipulations. These expenditures numbered 2572 and involved the issuance of 686 corporate checks. They were charged chiefly to corporate expense accounts for travel, automobile, entertainment and selling, and also to freight, office expense, engineering, contributions, professional services, factory expense, office equipment, dues and subscriptions, rent and advertising.

Government exhibits 4, 5, 6 set forth separately each of said expenditures for the years 1954, 1955 and 1956 respectively. Abbreviations used in these exhibits are explained as follows:

RT—Round Trip
OW—One Way
CHGS—Charges
AC—Account
PR—Pair
BRA—Brassiere
CTN—Carton
W-W—Wall to Wall
BEV—Beverages
HH—Household
PYMT—Payment

The government contends that this $212,328.97 was, and that defendant knew it to be, income, and the district court so found.

None of these items was charged to the personal account of taxpayer, which was carried on the corporate books under the title "L. A. Durant". It appears that this account had been maintained since the incorporation of United and even prior thereto during the period 1943 to 1946, when the business was operated as a sole proprietorship. During the entire prosecution period 1954-1956, this ac-

count was charged only three times for a total of $2,700.26 with purchases from the vendors who supplied the 2572 stipulated items involving the amount of the income not reported by defendant upon which this case rests. The government points out that, while there is evidence that defendant from time to time had given instructions on charging items to this account, there is no evidence cited to us that he ever gave explicit instructions to any corporate employee how to charge any of the 2572 items in issue. We have found none.

The government's position is that defendant knew that these items would not be charged to his account in the absence of instructions from him, that he intended they should be charged to corporate expense accounts, that he knew they constituted income to him and that he willfully suppressed this additional income to him in his joint income tax returns. The trial court so found, and the government submits its findings are amply supported by the evidence.

On the other hand, defendant insists that he had assumed that all items paid by the corporation for his personal benefit were being charged to his personal account. Although he testified that he could not recall telling anyone specifically to make a charge to his personal account, he testified that, if he made any withdrawals from the corportion, it was his understanding that he would have to repay them.

H. L. Oettinger, an experienced accountant, in 1946 was hired by defendant as overseer of the office. He had the responsibility of seeing that the distribution of expenses was proper. To him defendant delegated the administrative end of the business. In July of 1951 Walter B. Taibleson, a certified public accountant, became comptroller of United. He prepared tax returns for the years 1951 through 1955.

According to Frances Croson, the accounts payable clerk, two routines were used for handling bills. Generally they were received, analyzed and classified for distribution to the proper account and paid by check on a weekly basis, with the assistance of a National Cash Register office machine. The alternative routine was to expedite particular items on an individualized basis, in which case the checks were typed out as needed, and distributed once a month to various corporate accounts. These so-called "typed checks" had a detachable bottom portion for purposes of recording the expenditure as to payee, nature of purchase, classification, etc. Carl Olson, purchasing agent, received the bulk of the purchase bills for purpose of noting the proper account distribution. Other bills went to the specific persons to whom addressed or who were responsible for a particular account.

On classification questions, according to Miss Croson, in 1950 more bills without any indication as to distribution began coming through to her; that, prior to that, the number of bills, without any indication as to distribution was negligible; that some of the bills came to her and some to Oettinger, who would hand them to her; that, in the beginning, she would ask Oettinger how such bills would be distributed, and he invariably replied, "Use your best judgment"; that she never discussed procedures with defendant. During 1948, the bills generally came to her already bearing a notation of the proper account distribution. When items such as Marshall Field, Saks Fifth Avenue and Bonwit Teller, became larger and more numerous, she asked Oettinger, who told her to "handle them as best you can" and she distributed them as similar items had been handled before. Defendant, and Oettinger also, would ask her to make out "typed checks" to various persons, but neither ever told her how to charge them.

Occasionally it was defendant's practice to give bills to Taibleson or to Oettinger for payment, but not to indicate

how such bills should be charged. However, defendant did at times give instructions to charge himself personally or to a corporate project called "Caravan", based at Denver, which was engaged in development of electronic devices in connection with drilling of wells. In the absence of any such indication, the practice was to charge an expenditure to a corporate expense account.

As to many of the indictment items, defendant instructed his employees personally either to issue a check and return it to him; to issue a check in payment of a bill, where the only documentation of such bill was defendant's oral direction; to draw petty cash and give the funds to him; or to purchase merchandise for him to be disposed of at his personal direction or shipped where he designated. Defendant never did explain to employees that such items, all of which were herein stipulated as personal, were not business expenses but were personal to him.

Defendant also took blank checks with him on trips out of the city and, according to custom, needed no one's authority to do this. On occasion, he returned the bottom half of the check to the bookkeeping department. Of those items in evidence of such a nature, in only two instances did he indicate the purpose on the voucher portion as shown in the following two paragraphs. In all other instances he made no indication of the purpose for which the check was written. If Durant did not furnish this bottom half, or voucher portion, not only was there no way of knowing the purpose for which it was drawn, but the company was unaware it was issued until it cleared the bank.

Government exhibit 713 is a corporate check dated May 19, 1956, written by defendant in the amount of $576 to the order of John Engstead. The bill was incurred by Cynthia Brooks for photographs. Defendant entered the notation "Comm. Photo" on the voucher attached to the bottom of the check form and the item thereafter was entered to "office expense". Defendant on cross-exami-

nation said "Commerical Photo" may have been the name of the company and that he did not remember why he put on this notation.

Exhibit 357 is a corporate check written to cash by defendant on June 18, 1954, in the amount of $2,000 and given to Dorothy Raynor. Defendant admittedly made the notation "Spfld Ill—Eagle River Trip" on the voucher portion of the check and the item was thereafter charged to "travel expense". Defendant acknowledged the endorsement on this check was by Dorothy Raynor and that he "must have" given it to her. Although the item was stipulated as personal, defendant said this thought had not occurred to him.

Reports of business conditions were prepared daily and weekly and were submitted to defendant in that order. Defendant admittedly received them daily when in Chicago and by mail when absent.

Government exhibit 1086 snows that check disbursements for defendant's personal benefit and so charged to his L. A. Durant account, were substantially all reflected on the daily reports with the designation "L. A. D." in the portion entitled "Disbursement Summary". Defendant testified this notation "L. A. D." on daily report items meant that they were being charged to his personal account.

Exhibit 1087 is a sample daily report for July 26, 1956, which, in the summary of disbursements portion, contains the following entry "L. A. D. CKS. of 6-27 * * * Travel Exp. 9,500.00. This $9,500 is the sum of exhibits 141 and 143. Exhibit 141 is a $3,000 check to cash dated June 27, 1956. Exhibit 143 is a $6,500 check issued by defendant to a Honolulu jewelry firm on June 27, 1956, in payment for pearl jewelry purchased by defendant as gifts for friends. The $9,500 was charged to corporation "travel expense".

As the government points out, of a total of $56,304.95 in check disbursements charged to the L. A. Durant account in 1956, the daily reports reflect $55,124.63. This

$56,304.95 was effected by the issuance of 25 checks, whereas 319 checks were issued to effect the personal disbursements stipulated in government exhibit 6 during 1956, none of which appeared in the daily reports as "L. A. D." account charges. These figures have not been questioned by defendant.

In 1951, agent Zivin examined United's and defendant's returns for 1949 and 1950. He made no third-party investigation of certain unsubstantiated expenses disallowed to the corporation, and also could not readily determine from the corporate books which were items of expenditure made for the benefit of defendant. He reviewed these items several times with Oettinger and Durant to determine their true nature. In December 1951, in a final conference Zivin so stated to Oettinger and defendant, with a warning that this practice had to be stopped, to which defendant replied, that if it had been done it was a mistake and that the items should have been charged to his personal account.

Zivin's itemized report of the corporation's personal and unsubstantiated expenses which he charged to defendant, showed the following totals:

L. A. Durant

	Personal	No Substantiation
1949	$ 3,055.50	$47,400.00
1950	39,534.71	74,342.86

Zivin charged both categories to defendant as dividends. Sworn protests were filed in which defendant alleged that, with the exception of nine items, all disallowed expenses were exclusively devoted to official corporate expense by defendant.

The case was reassigned to revenue agent Wagar, who consulted Zivin's reports and examined the years 1951, 1952 and 1953. Without any third-party investigation, Wagar perpared reports dated April 26, 1954, proposing

certain adjustments covering the years 1949 through 1953, and disallowing to the corporation certain of the expenses claimed and charging to defendant as dividends certain amounts for each year. Before submitting his report, Wagar discussed with defendant the practice of taking corporate tax deductions for personal expenditures and said this practice was improper. Defendant did not explain how they came to be charged to corporate expense accounts. Wagar's report contained an itemized listing of corporate expense items determined to be personal in nature. Defendant discussed with the comptroller, Taibleson, the selling and travel expenses disallowed by Wagar.

The proposed assessments were settled by agreements for payments of additional corporate and personal taxes, totaling about $600,000.

Thereafter, defendant's personal expenditures continued to be paid by and charged to the corporation. During 1954, 1955 and 1956, $79,104.95 in personal items was actually disbursed to vendors who had been identified with dividend items charged to defendant in the prior audits. Defendant admitted that he made no changes in the accounts payable routine.

Defendant himself testified that in 1951 or 1952 he met with Agent Zivin and that, some unfixed date in 1954, he had a conversation with Agent Wagar. He admitted that there was a discussion with Zivin about personal items that the corporation had paid for. He "assumed" that he knew what the discussion with Zivin "was all about."

He testified that he read and signed a protest against Zivin's ruling, prepared by his lawyers.

1. We first dispose of the contention of defendant that, if he had an intent to repay United Manufacturing Company for personal expenses paid by it on his behalf, the fact that they were not charged to his personal account has no effect, but they are loans. He cites *Estate of Helene*

Simmons, 26 T. C. 409 (1956), *Carl L. White*, 17 T. C. 1562 (1952), and *Walter Freeman*, 16 T. C. M. 71 (1957).

In the case at bar, the district court found that the record is clear that at no time were the payments in question ever considered as loans by the parties. The corporation did not carry them on its books as notes or accounts receivable; no notes or other evidence of loans were ever executed by the defendant; no interest was ever paid to the corporation by the defendant; no maturity or repayment date was set; no repayment was made; defendant never advised any of the responsible subordinates that the payments were to be treated as loans and charged to his personal account; in fact, no action was taken by either the defendant or the corporation which would indicate that the payments were loans.

The district court found that the payments made by the corporation in the taxable years for defendant's benefit were income to defendant, which was known to defendant. This finding is supported by the uncontradicted evidence in the record, most of it stipulated.

Accordingly we hold that the payments by the corporation for the benefit of defendant were not loans by it defendant, but were income.

2. Defendant insists that the statute here involved, 26 U. S. C. A. § 7201, requires proof of willfulness by the defendant.

That section reads:

> Any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof shall, in addition to other penalties provided by law, be guilty of a felony * * *.

Defendant submits that the most that can be inferred from the evidence in this case is a certain amount of laxity,

but his counsel urges that any amount of laxity does not constitute the requisite willfulness.

As an abstract proposition, we would agree that no amount of laxity in and of itself constitutes willfulness. However, in the case at bar, we believe that the district court properly recognized the additional factors revealed by the records, tending to prove a willful intent: (a) defendant knew the corporation was paying his expenses, (b) the payments were not considered loans by the parties, (c) defendant knew the corporate payments were income to him; and therefore properly found that defendant willfully failed to include them in his returns.

As we have indicated, the events following the prior audits for 1949-1953 served to clearly warn defendant of his duty to report as his personal income the charges of indebtedness incurred by him and paid by the corporation. Moreover, his failure to indicate on many of the expenditure vouchers any notation indicating appropriate classifications leading to a proper charge to him personally, also tends to support the finding of willfulness.

His continuous failure to see that the warnings of Zivin and Wagar were heeded might reasonably be expected to result in a continuation of the practice of charging his personal obligations to the corporation.

We are not concerned here with any ethical question as to the propriety of defendant's benefactions to various ladies. No requirement of federal tax laws bars such nurture of cordial relations with them. Yet the court, as the trier of the facts, had a right to consider the repeated charges to the corporation for gifts by defendant to feminine acquaintances despite the previous warnings, and to find that he had deliberately and willfully continued to permit the making of such improper charges. By the sequence of events, the continuation of that practice, which in prior years may have resulted from defendant's negli-

gence, in the years 1954, 1955 and 1956 became deliberate and willful.

Whether defendant willfully attempted to defeat and evade taxes in this case presented a question for the trier of the facts. There was substantial evidence before the court to support the result which it reached. The credibility of defendant as a witness and the weight to be given to his testimony were peculiarly within the knowledge of the court, which had an opportunity to observe his demeanor while testifying. On appeal, we are forced to hold, as we do, that there was sufficient evidence viewed in the light most favorable to sustain the court's finding, to prove the charge upon which defendant was tried. *Blauner* v. *United States*, 8 Cir., 293 F. 2d 723, 725 (1961); *United States* v. *Dudley*, 2 Cir., 260 F. 2d 439, 440 (1958); *United States* v. *Tutino*, 2 Cir., 269 F. 2d 488, 490 (1959). Cf. *Wolfe* v. *United States*, 6 Cir., 261 F. 2d 158, 160 (1958).

For these reasons, the judgment from which defendant has appealed is affirmed.

JUDGMENT AFFIRMED.

A true Copy:
Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit.

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

Chicago 10, Illinois

Wednesday, November 6, 1963

Before:

HON. JOHN S. HASTINGS, *Chief Judge*
HON. ELMER J. SCHNACKENBERG, *Circuit Judge*
HON. LATHAM CASTLE, *Circuit Judge*

No. 14005

UNITED STATES OF AMERICA, *Plaintiff-Appellee,*

v.

LYNDON A. DURANT, *Defendant-Appellant.*

Appeal from the United States District Court
for the Northern District of Illinois, Eastern Division

This cause came on to be heard on the transcript of the record from the United States District Court for the Northern District of Illinois, Eastern Division, and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this court that the judgment of the said District Court in this cause appealed from be, and the same is hereby, AFFIRMED, in accordance with the opinion of this Court filed this day.

APPENDIX B

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 61 CR 260

UNITED STATES OF AMERICA, *Plaintiff*,

v.

LYNDON A. DURANT, *Defendant*.

Special Findings of Fact and Opinion

This Court, sitting without a jury, having heard all of the testimony, examined all the evidence, the indictment numbered 61 CR 260, the bill of particulars, the stipulations of the parties filed of record, and the written and oral arguments of counsel in this cause, upon request of the defendant, pursuant to rule 23(c), Federal Rules of Criminal Procedure, hereby finds the following facts to be true:

1. On April 15, 1955, the defendant Lyndon A. Durant, filed and caused to be filed with the District Director of Internal Revenue for the Chicago Internal Revenue District, at Chicago, Illinois, a joint income tax return on behalf of himself and his wife, Kathleen Durant, for the calendar year 1954, which return was prepared by Herbert L. Oettinger and signed by the defendant. The total income tax paid by the defendant for the calendar year 1954 was $132,953.48, the amount of tax stated in the said return to be due and owing upon the stated joint taxable income of $273,802.81 of him and his wife, which joint taxable income was earned and/or derived by him in the said calendar year.

2. On April 9, 1956, the defendant Lyndon A. Durant, filed and caused to be filed with the District Director of Internal Revenue for the Chicago Internal Revenue District, at Chicago, Illinois, a joint income tax return on behalf of

himself and his wife, Kathleen Durant, for the calendar year 1955, which return was prepared by Herbert L. Oettinger and signed by the defendant. The total income tax paid by defendant for the calendar year 1955 was $29,136.15, the amount of tax stated in the said return to be due and owing upon the stated joint taxable income of $64,332.54 of him and his wife, which joint taxable income was earned and/or derived by him in the said calendar year.

3. On April 15, 1957, the defendant Lyndon A. Durant, filed and caused to be filed with the District Director of Internal Revenue for the Chicago Internal Revenue District, at Chicago, Illinois, a joint income tax return on behalf of himself and his wife, Kathleen Durant, for the calendar year 1956, which return was prepared by Bansley and Kiener, certified public accountants, and signed by the defendant. The total income tax paid by the defendant for the calendar year 1956 was $31,859.87, the amount of tax stated in the said return to be due and owing upon the stated joint taxable income of $72,346.08 of him and his wife, which joint taxable income was earned and/or derived by him in the said calendar year.

4. The United Manufacturing Company, an Illinois corporation (hereinafter called "United"), of which the defendant Lyndon A. Durant, was the President and sole stockholder, during each of the calendar years 1954, 1955 and 1956, made expenditures for or on behalf of the defendant and for his personal economic benefit in the following total amounts:

1954	$ 51,716.17
1955	66,877.19
1956	93,735.61

5. Each of the expenditures by United reflected in finding four hereof were either recorded in the records of United as expenses of the said corporation and deducted by the

said corporation as business expenses of the said corporation in each of its corporate income tax returns filed for the respective calendar years 1954, 1955 and 1956, or were recorded as an acquisition of an asset by the said corporation, which was thereafter depreciated by it and the said depreciation then deducted by the corporation on its income tax returns as an expense. None of the aforesaid expenditures in fact constituted an expense or acquisition of assets of United and were all of a personal economic benefit to the defendant.

6. Of the expenditures made by United reflected in finding four hereof, and all of which expenditures were of a personal economic benefit to the defendant in the calendar years 1954, 1955 and 1956, respectively, none were included in the amount of joint taxable income stated in the joint income tax returns filed by the defendant on behalf of himself and his wife for the calendar years 1954, 1955 and 1956, respectively.

7. The payments made by United in the years 1954 to 1956, referred to in finding four hereof, for the defendant's personal economic benefit were income to the defendant in each of the respective amounts for each of the respective years.

8. The defendant, Lyndon A. Durant, as President of United, was its chief executive officer as well as its chief engineer, designer and electronic specialist. He delegated authority for the supervision of the administrative affairs of the corporation to Herbert L. Oettinger, Vice President of the corporation, who was responsible for the keeping of all corporate books of account during the years 1954, 1955 and 1956. During the years 1954, 1955 and 1956, the corporation employed one, Walter Taibleson, a certified public accountant, as controller, who was subordinate to Oettinger, the Vice President, as was Miss Frances Croson, who was in charge of the accounts payable.

9. The books of account of the corporation contained an account entitled "L. A. Durant." During the years 1954, 1955 and 1956, United made expenditures for or on behalf of the defendant for his personal use and benefit aggregating $815,021.08 of which $602,692.11 was charged to the personal account entitled "L. A. Durant" and the agreegate of $212,328.97 reflected in finding four hereof was charged as set forth in finding five hereof.

10. Commencing in December 1951, the corporate income tax returns of United for the years 1949 and 1950 were examined by Internal Revenue Agent Alfred E. Zivin. Agent Zivin questioned four general categories of items in the corporation's books and records of account, one of which was the use of corporate funds for personal expenses. In connection with his audit of the corporation's returns, Agent Zivin had several conferences at which both the defendant and Oettinger were present and in which the question of charging personal expenses to the corporation was discussed. On December 23, 1951, Agent Zivin had a final conference with the defendant and Oettinger, at which all four categories of items were discussed and the agent advised the defendant and Oettinger the the practice of charging personal expenses to the corporation should be stopped. The defendant replied that if there were personal expenses charged to the corporation, they should be charged to his personal account.

11. In February of 1954, a second Internal Revenue Agent, William H. Wagar, examined the returns of United for the years 1949 through 1953. He too questioned the same four general categories which Agent Zivin had raised and disallowed substantial personal expenses of the defendant which had been charged to the corporation in each of the five years. Agent Wagar likewise had conferences with the defendant and Oettinger during the course of which he informed the defendant that it was improper for him to charge personal expenses to the corporation al-

though Agent Wagar did not discuss the specific items with the defendant but discussed them with Oettinger.

12. Neither the defendant nor anyone else instructed the controller Taibleson to make any changes in the bookkeeping and accounting practices of the corporation after either agent's examination. On a number of occasions, the defendant brought invoices and bills to Taibleson and directed him to pay the same without designating any account to which they were to be charged. In the absence of a specific direction by defendant to charge a particular item to his personal account, it was the established practice of the corporation to charge such items to various corporate accounts.

13. On a number of occasions during the years 1954 through 1956 the defendant instructed the purchasing agent of the corporation, Carl J. Olson, to purchase merchandise for him. Ordinarily there would be no formal requisition or purchase order and the merchandise would be disposed of as directed by the defendant. On no occasion did the defendant instruct Olson to charge the purchases to his personal account and, pursuant to the established practice of the corporation, Olson charged such purchases to various corporate accounts. On some occasions the defendant would instruct Olson to make purchases for a separate corporate project which was known as "Caravan" and the defendant would indicate that such purchases were to be charged to the Caravan account.

14. The defendant knew at the time he filed his income tax returns for each of the years 1954 to 1956, respectively, that he had taxable income as a result of the payments made by United for his personal economic benefit as set forth in finding four hereof.

15. Each of the income tax returns filed by the defendant for the years 1954 to 1956, as set forth in findings 1, 2 and 3 hereof, were false when filed by the defendant and

the defendant knew them to be false at the time of their filing.

16. The defendant wilfully and knowingly attempted to evade and defeat a part of the income tax due and owing by him and his wife to the United States of America for each of the years 1954, 1955 and 1956 respectively, by knowingly and intentionally filing false and fraudulent joint income tax returns on behalf of himself and his wife, Kathleen Durant, wherein, in each of the said returns, he knowingly and intentionally falsely stated their joint taxable income and the income tax due and owing thereon. This conduct on the part of the defendant constituted, in each of the years 1954, 1955 and 1956, a violation of section 7201, Internal Revenue Code of 1954, 26 U.S.C. section 7201.

Wherefore, the Court finds the defendant, Lyndon A. Durant, guilty as charged in each of Courts 1, 2 and 3 of indictment 61 CR 260.

OPINION

The defendant, Lyndon A. Durant, is charged in a three count indictment with a wilful and knowing attempt to evade and defeat the income taxes due and owing for himself and his wife for each of the years 1954, 1955 and 1956, by causing to be filed false and fraudulent income tax returns for each of such years, in violation of section 7201 of the Internal Revenue Code of 1954, 26 U.S.C. section 7201.

It has been stipulated by the parties that the United Manufacturing Company (hereinafter called "United"), of which the defendant was the sole stockholder and principal executive officer during the years 1954, 1955 and 1956, made expenditures for or on his behalf and for his personal economic benefit in an aggregate amount of $212,328.97 as follows:

1954	$ 51,716.17
1955	66,877.19
1956	93,735.61

It has been further stipulated that all of these items were charged to various corporate accounts and that none of them were reported as income by the defendant and his wife in their joint returns for the years in question. During the same period the corporation made additional expenditures for or on behalf of the defendant and for his personal economic benefit in an aggregate of $602,692.11 which were charged to a personal account on the books of the corporation entitled "L. A. Durant."

On behalf of the defendant, it is urged that while there is no dispute that the $212,328.97 was paid for his personal benefit by the corporation and charged to corporate accounts during the relevant years, this was done without his personal knowledge, and he assumed that these items, together with the $602,692.11, were all being charged to his personal account. Accordingly, it is contended that (1) the amounts in question were loans and did not constitute income to the defendant and (2) he lacked the requisite criminal intent to sustain a conviction under the applicable section of the Internal Revenue Code.

With respect to the first contention, the record is clear that at no time were the payments in question ever considered as loans by the parties. The corporatin did not carry them on its books as notes or accounts receivable; no notes or other evidence of loans were ever executed by the defendant; no interest was ever paid to the corporation by the defendant; no maturity or repayment date was set, no repayment was made; defendant never advised any of the responsible subordinates that the payments were to be treated as loans and charged to his personal account; in fact, no action was taken either by the defendant or the corporation which would indicate that the payments were loans.

If the defendant intended these transactions to be loans, it behooved him to insure that the corporate records so reflected them. Otherwise, there would be no way in which the corporation could ever know what amounts were owed to it. Where, as here, substantial amounts are charged to a personal loan account at the instructions of the principal officer and sole stockholder, the only possible inference is that additional items not so charged because he gave no such instructions were not intended to be and were not loans.

The second question, that of whether or not the defendant had the requisite intent, presents in and of itself, two questions, first, whether he knew that the corporation was paying his personal expenses, and, second, if he did, whether he knew that such items were income to him which should have been included in his personal income tax return and wilfully or deliberately failed to include them therein.

In support of the contention that he did not know the corporation was paying his personal expenses, the defendant has introduced testimony establishing that although he was the principal executive officer of the corporation, he delegated the responsibility for the maintenance of the books and records and the administration of the company's office to subordinates on whom he relied for the proper handling thereof.

The record also discloses that the defendant had been advised by two internal revenue agents, who audited the corporation's and the defendant's income tax returns for prior years, that the charging of personal expenses to corporate expense accounts was improper and should be stopped but that the defendant did not instruct his subordintes to make any changes in the established and long-standing corporate practice. That practice was to charge any bill or invoice submitted by the defendant to a corporate account unless he specifically designated that it should

be charged otherwise. There is, however, no evidence that the defendant at any time instructed his subordinates to adopt this practice and to charge his personal expenses to corporate accounts.

It is difficult to believe, though, that the defendant was unaware of what was actually taking place. It has been stipulated, for example, that during the years in question he gave credit cards on various petroleum companies such as Standard Oil, Shell, Phillips, Pure Oil, etc., to his wife, his sister and a number of personal friends, authorizing them to make purchases to be charged to the account of the corporation. Similarly, he instructed the purchasing agent of the corporation to make numerous purchases of merchandise unrelated to the business activities of the corporation and to be delivered to relatives and personal friends while at no time instructing that such purchases be charged to him personally. The substantial number and volume of such transactions alone, two thousand five hundred and seventy-two in the three years, compel the conclusion that the defendant was aware of them and the manner in which they were being handled on the corporation's books.

In addition to the foregoing, the defendant on a number of occasions personally issued corporate checks to pay for his personal expenses with either no indication on the voucher poriton thereof that they were personal or, in some instances, made notations such as "commercial photos" or "Springfield, Illinois—Eagle River Trip" which were suscept ble of the interpretation that they were proper corporate expenses. Nor did he ever advise his subordinates that any of such checks were in fact personal.

There remains then the question of whether defendant knew that the payments by the corporation for his personal benefit were income to him which he wilfully or deliberately failed to include in his personal returns for the years 1954-1956. That such payments were, in law, income

to the defendant must likewise have been known by him since they were similar in nature to the more than $105,000.00 of disallowed corporate expenses previously charged to him as income by the revenue agents in their audits of the years 1949 through 1953.

Intent or wilfulness is, of course, a subjective fact and may be determined either from direct proof of statements or acts or by inference from circumstantial evidence. *U. S. v. Paschen*, 7 Cir. 1934, 70 F. 2d 491.

It is elementary that negligence or carelessness are not sufficient to constitute the requisite criminal intent. *Gaunt v. U. S.*, 1 Cir. 1950, 184 F. 2d 284. Nor can intent be infererd from the mere understatment of income or from the failure to report income which is not commonly recognized as such in the normal affairs of men. *U. S. v. Bridell, et al.*, D.C. N.D. Ill. 1960, 180 F. Supp. 268.

Defendant here, however, after being warned by two revenue agents that the charging of personal expenses to corporate accounts and the failure to report such items as income in his joint returns was improper, made no change whatsoever in the challenged practices. What may have been negligence or mere understatement of income in the earlier years can hardly be so considered in later years after the agents' warnings. The only reasonable inference from defendant's conduct is that he deliberately and wilfully continued practices which he had been advised were improper and the effect of which was substantially to understate his taxable personal income.

There is a point of repetition at which action originally careless or negligent becames deliberate and wilful. The defendant passed that point when, after warnings by two revenue agents, he did nothing but continue the improper and challenged practices.

In the light of all of the foregoing, I am satisfied beyond a reasonable doubt that the defendant is guilty as charged

in each of the three counts of the indictment. Judgment will be entered accordingly.

ENTER:

/s/ HUBERT L. WILL
Judge

Dated: October 1, 1962

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statute involved	2
Statement	2
Argument	7
Conclusion	10

CITATIONS

Cases:

Cave v. *United States*, 159 F. 2d 464	8
Grant v. *United States*, 184 F. 2d 284	9
Pappas v. *United States*, 216 F. 2d 515	9
Rick v. *United States*, 161 F. 2d 897	8
Smith v. *United States*, 348 U.S. 147	8
Spies v. *United States*, 317 U.S. 492	8
United States v. *Allen*, 44 A.F.T.R. 894	9
United States v. *Beacon Brass Co.*, 344 U.S. 43	8
United States v. *Croessant*, 178 F. 2d 96, certiorari denied, 339 U.S. 927	8
United States v. *Pechenik*, 236 F. 2d 844	9
United States v. *Rosenblum*, 176 F. 2d 321	8

Statute:

Internal Revenue Code of 1954, Sec. 7201 (26 U.S.C. 1958 ed., Sec. 7201)	2, 8

726-124—64

In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 875

LYNDON A. DURANT, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. 1a–11a) is reported at 324 F. 2d 859. The opinion of the district court (Pet. 13a–23a) is reported at 208 F. Supp. 890.

JURISDICTION

The judgment of the court of appeals was entered on November 6, 1963 (Pet. 12a), and a petition for rehearing was denied on December 30, 1963. On January 20, 1964, Mr. Justice Clark extended the time for filing a petition for a writ of certiorari to February 28, 1964, and the petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the evidence was sufficient to support petitioner's conviction for willful tax evasion.

STATUTE INVOLVED

Internal Revenue Code of 1954:

> SEC. 7201. ATTEMPT TO EVADE OR DEFEAT TAX.
>
> Any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, shall be fined not more than $10,000, or imprisoned not more than 5 years, or both, together with the costs of prosecution.

(26 U.S.C. 1958 ed., Sec. 7201.)

STATEMENT

Having waived trial by jury, petitioner was found guilty after a trial before the court in the Northern District of Illinois on three counts of having willfully attempted to evade and defeat individual income taxes for the years 1954, 1955, and 1956 by filing false and fraudulent tax returns for those years. The indictment alleged that the net income and taxes reported on petitioner's returns were understated as follows:

Year	Net income		Income tax	
	Reported	Corrected	Reported	Corrected
1954	$273,803	$321,909	$102,963	$166,311
1955	66,855	151,156	20,140	75,689
1956	72,346	165,874	31,800	95,884
Total	413,982	638,939	154,903	337,884

Petitioner was sentenced to concurrent 60-day prison terms and to fines totaling $15,000 (Pet. 3). The court of appeals affirmed the conviction.

The evidence supporting the verdict may be summarized as follows: Petitioner operated the United Manufacturing Co., which was engaged in the production of pin-ball machines and other games, first as a sole proprietorship and, after January 1946, as a corporation. Petitioner was the sole stockholder, president and treasurer of the corporation, and he had full control over its operations (R. 10, 18, 69, 116).[1] Only petitioner and Herbert Oettinger, who was employed as the corporation's vice-president and secretary, were authorized to sign corporate checks (R. 17, 55). Walter B. Taibleson was comptroller and head of the corporation's accounting department (R. 71). Late in 1951 a Treasury agent commenced an investigation of the 1949 and 1950 returns of petitioner and the corporation (R. 115–116). Upon discovering that in many instances petitioner's personal expenses had been charged on the corporate books, the agent cautioned petitioner to stop the practice (R. 129, 160). He also advised petitioner that such payments made by the corporation for petitioner's personal expenses constituted income to petitioner (R. 161). Petitioner replied that such items should have been charged by the corporation to his personal account (R. 129, 160). When the agent brought the matter of these improper charges to Oettinger's attention, Oettinger shrugged his shoulders and replied that petitioner "was the boss" (R. 130).

[1] "R." refers to petitioner's appendix in the court of appeals.

Thereafter, a second revenue agent made an investigation of the individual and corporate returns for the years 1951, 1952, and 1953 (R. 168–171, 334–335, 412). He too discovered that many corporate checks issued in payment of petitioner's personal expenditures had been charged to corporate expense accounts in those years (R. 174–175), and advised petitioner and Oettinger that the corporate deductions were improper (R. 179). Petitioner conceded that these items constituted dividends to him and agreed to the assessment of tax deficiencies (R. 187). In August 1954—before any of the tax returns involved in the present case were filed—petitioner paid $127,963.82 in tax deficiencies on his individual returns for the years 1949 through 1953 and additional tax deficiencies on the corporate returns for the same years (R. 14–15).

Taibleson testified that when he was first employed by the corporation in 1951 Oettinger advised him that it was the usual practice to charge all incoming bills to corporate expense accounts, but that there were occasions when petitioner would instruct Taibleson to charge particular items to his personal account (R. 53, 59). He further testified that petitioner ordinarily brought corporate bills to him, laid them on Taibleson's desk and told him to pay them (R. 56–57). When petitioner wanted a particular item charged to his personal account he would orally instruct Taibleson to this effect (R. 65); unless such oral instruction was given all bills would be charged to corporate expense accounts (R. 48–49, 65–66).

Taibleson also testified that shortly after the investigation made by the second revenue agent, Oet-

tinger told him: "Well, I guess we are not going to be charging [petitioner] for some of these personal bills" (R. 445). This statement was made by Oettinger notwithstanding the agent's specific warning a short time before that if the practice of charging petitioner's personal bills to business expense were continued, the government would "take a more severe position * * *" (R. 446). No one instructed Taibleson to make any changes in the corporation's bookkeeping system, and so far as Taibleson knew petitioner issued no instructions to anyone to change the system (R. 54–55, 60, 64–65, 329).

In 1957 Treasury agents began an investigation of the tax returns of petitioner and the corporation for the years 1954, 1955, and 1956. In examining the corporate books and records the agents discovered many charges to expense for which no underlying documents were available. A team of agents thereupon made between 300 and 350 inquiries of third parties to determine the nature of these expenses (R. 206–210). It was learned that corporate expense accounts had been charged for many gifts of money (ranging from $1,000 to $3,000) made by petitioner to his friends; for personal merchandise purchased in department stores by petitioner's friends; for charges on gasoline credit cards given by petitioner to eleven friends; and for such other personal purchases as clock radios, television sets, hosiery, home furniture (including a piano), a kitchen range, a power mower, electric fans and a hair dryer (R. 9–10, 21–46, 100–109). There were 2,572 such items improperly charged to corporate expense accounts

during the three-year period, and their cost value was $212,328.97 (R. 236–237). The corporate records with respect to most of these items failed to disclose that they were personal in nature, rather than being legitimate business expenses (R. 237).

The district court issued special findings of fact and a supporting opinion (Pet. 13a–23a; R. 456–466). It found, *inter alia,* (1) that in 1954–1956 the corporation had made expenditures for petitioner's "personal economic benefit" in amounts exceeding $51,000, $66,000, and $93,000, respectively; (2) that these expenses were reflected in the corporation's books as business expenses or as acquisitions of depreciable business assets; (3) that these expenses were, in fact, income to petitioner which was not reported on his tax returns; (4) that petitioner had been warned by two revenue agents that it was improper for him to charge personal expenses to corporate accounts; (5) that petitioner did not change the bookkeeping and accounting systems after these warnings; (6) that petitioner submitted bills to Taibleson and gave purchase instructions to the corporation's purchasing agent without telling them to charge specific personal items to his personal account; (7) that petitioner "knew at the time he filed his income tax returns for each of the years 1954 to 1956, respectively, that he had taxable income as a result of the payments made by United for his personal economic benefit * * *"; and (8) that such income tax returns "were false when filed * * * and [petitioner] knew them to be false at the time of their filing." In the supporting opinion, the court observed that the substantial number and

volume of the expenses incurred by the corporation for petitioner's personal benefit "compel the conclusion that [petitioner] was aware of them and the manner in which they were being handled on the corporation's books." Having been warned by the agents that such expenses were income to him, and having been previously charged for similar expenses made during earlier tax years, petitioner was held by the district court to have had knowledge that such items should have been included on his personal tax returns. Accordingly, the court concluded that "[t]he only reasonable inference from defendant's conduct is that he deliberately and willfully continued practices which he had been advised were improper and the effect of which was substantially to understate his taxable personal income."

ARGUMENT

The only issue in this case is whether the evidence was sufficient to sustain the district court's conclusion that petitioner's attempts to evade personal income tax were done "willfully." The decision does not, as petitioner contends, sweepingly subject corporate executives to criminal liability for minor imperfections in the bookkeeping services performed by their employees. Rather, it permits a district court to infer that evasion of tax was deliberate and willful from evidence demonstrating a consistent and aggravated course of conduct which has been continued in the face of warnings by government agents. The decision was correct and does not, therefore, call for further consideration by this Court.

1. Petitioner's contention that the court of appeals' decision is irreconcilable with *Spies* v. *United States*, 317 U.S. 492, is totally without merit. In *Spies* the failure to file any return whatever was held to be covered by the misdemeanor provision which is presently Section 7203. *Spies* certainly did not hold, nor did it even suggest, that the actual filing of a false or fraudulent return, if done with the requisite intent, would not be punishable as a felony under the present Section 7201. Indeed, it is well-established that such false filing is precisely the kind of "affirmative" conduct which Section 7201 was meant to prohibit. *United States* v. *Beacon Brass Co.*, 344 U.S. 43, 46; *Smith* v. *United States*, 348 U.S. 147, 159; *Cave* v. *United States*, 159 F. 2d 464, 466 (C.A. 8th); *United States* v. *Rosenblum*, 176 F. 2d 321, 329–330 (C.A. 7th); *United States* v. *Croessant*, 178 F. 2d 96 (C.A. 3d), certiorari denied, 339 U.S. 927. In *Rick* v. *United States*, 161 F. 2d 897, 898 (C.A. D.C.), it was noted that the filing of a false return is "the most common and also the most flagrant method of willfully attempting to defeat or evade an income tax." Consequently, the "affirmative" conduct required by *Spies* was fully satisfied here by petitioner's filing of the false returns.

2. There is no conflict between this decision and those in other circuits, as petitioner alleges (Pet. 17–18). The district court and the court of appeals recognized here, as did the courts in the cases cited

by petitioner, that willfulness requires more than a showing of carelessness, negligence, or inadvertence.[2] Applying the proper standard (Pet. 22a; R. 465), the district court correctly determined that petitioner, who was the sole stockholder of the corporation and had complete control over its operations and its employees, had acted willfully by intentionally continuing a practice which had been condemned by revenue agents and which petitioner had personally acknowledged as wrongful by voluntarily paying the tax deficiencies assessed upon him and the corporation for earlier years.

3. The evidence in this case presents a picture which is markedly different from the hypothetical instances of "improper and negligent bookkeeping practices" suggested as analogies by petitioner (Pet. 10–11). Petitioner here had knowledge of the misuse of the corporate books and had been warned by government agents of the consequences of permitting it

[2] In *Pappas* v. *United States*, 216 F. 2d 515 (C.A. 10), and in *Gaunt* v. *United States*, 184 F. 2d 284 (C.A. 1), the courts of appeals sustained instructions by trial courts which defined "willfully" in these terms. In *United States* v. *Pechenik*, 236 F. 2d 844 (C.A. 3), the proof failed to support an inference that the defendant was aware of the corporation's improper accounting practices, and in *United States* v. *Allen*, 44 A.F.T.R. 894, 896 (S.D. Cal.), it was found that a disgruntled employee had falsified the books without the defendant's knowledge. None of these cases supports petitioner's contention that knowledge of the sort shown here, together with continued disregard of the law, is insufficient to sustain the inference of willfulness.

to continue. Moreover, throughout the relevant years petitioner was receiving daily and weekly reports which showed, *inter alia*, the amount of corporate checks "released" each day and the charges to petitioner's personal account on the corporation's books (R. 66–67, 84, 87, 405–406). Notwithstanding the warnings and knowledge he had, petitioner made no change in the bookkeeping system. Instead he amassed, over the course of three years, more than $212,000 in total personal expenses which were paid by the corporation and which appeared on its books as ordinary business expenses. This deliberate course of conduct was patently a far cry from mere "incomplete and imperfect" bookkeeping practices. It fully justified the district court's conclusion that petitioner had acted deliberately and willfully.

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be denied.

Respectfully submitted.

ARCHIBALD COX,
Solicitor General.
LOUIS F. OBERDORFER,
Assistant Attorney General.
JOSEPH M. HOWARD,
RICHARD B. BUHRMAN,
Attorneys.

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